

May 11th, 2011



GasMart 2011

Presented by Paul M. Corby
Senior Vice President
Planalytics Inc;



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So, what are you all doing here?

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Have you learnt anything yet???

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Tell me something I don't know!!!

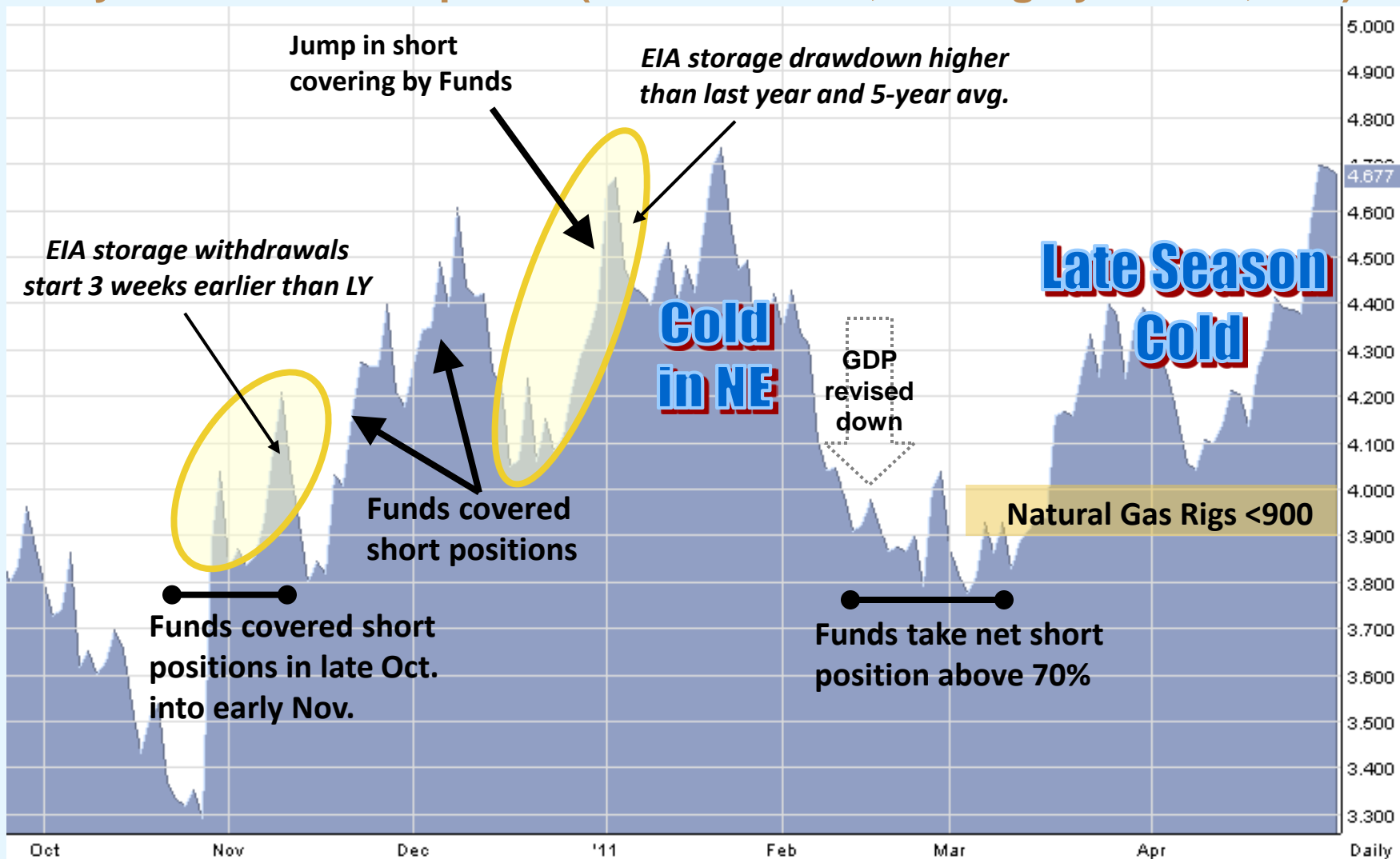
- Commodity (natural gas) markets have become institutionalized.
 - Have become part of regular trading portfolio
 - No longer considered an “alternate” asset
- Traded by mutual funds, pension funds, hedge funds, etc.
- This has profound impact on natural gas markets and the people who use them.
- Buying/hedging in this environment.

Commodities traded by contract volume in the U.S.

1. **Crude Oil**
2. **Natural Gas**
3. **Heating Oil**
4. Sugar - World #11
5. **RBOB Gasoline**
6. Gold
7. Corn
8. Wheat
9. Soybeans
10. Copper
11. Soybean Oil
12. Silver
13. Cotton
14. Cocoa

A More Complex Market

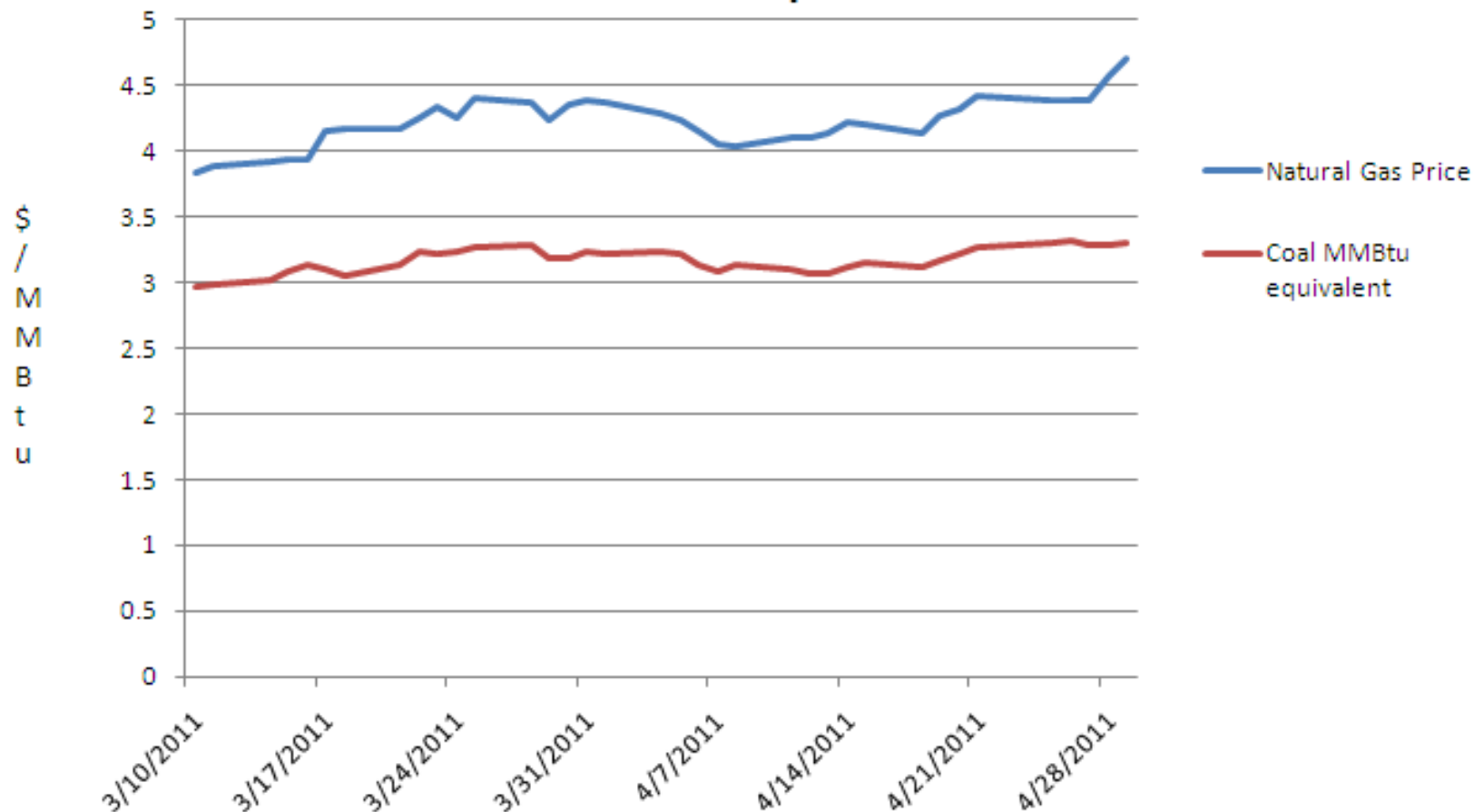
Many variables drive prices (fundamentals, trading dynamics, etc.)



Price Drivers



Coal/Gas MMBtu Equivalent



Price Drivers

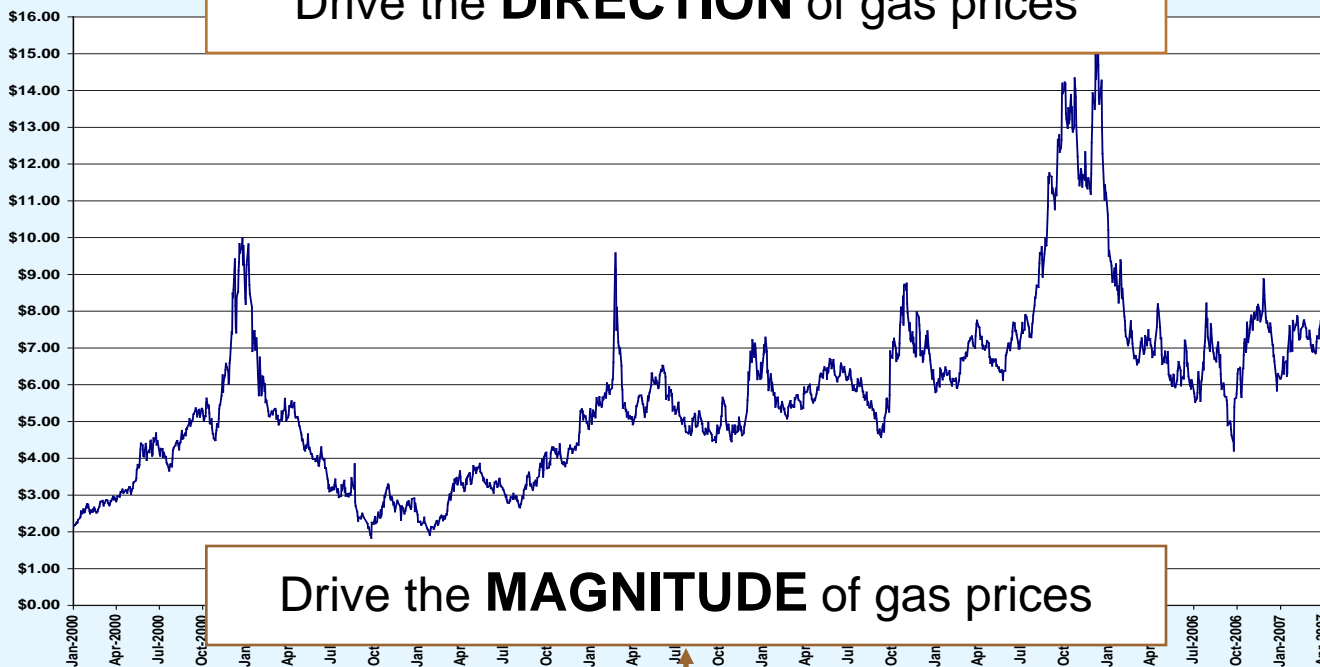


FUNDAMENTALS

TECHNICALS

MARKET DYNAMICS

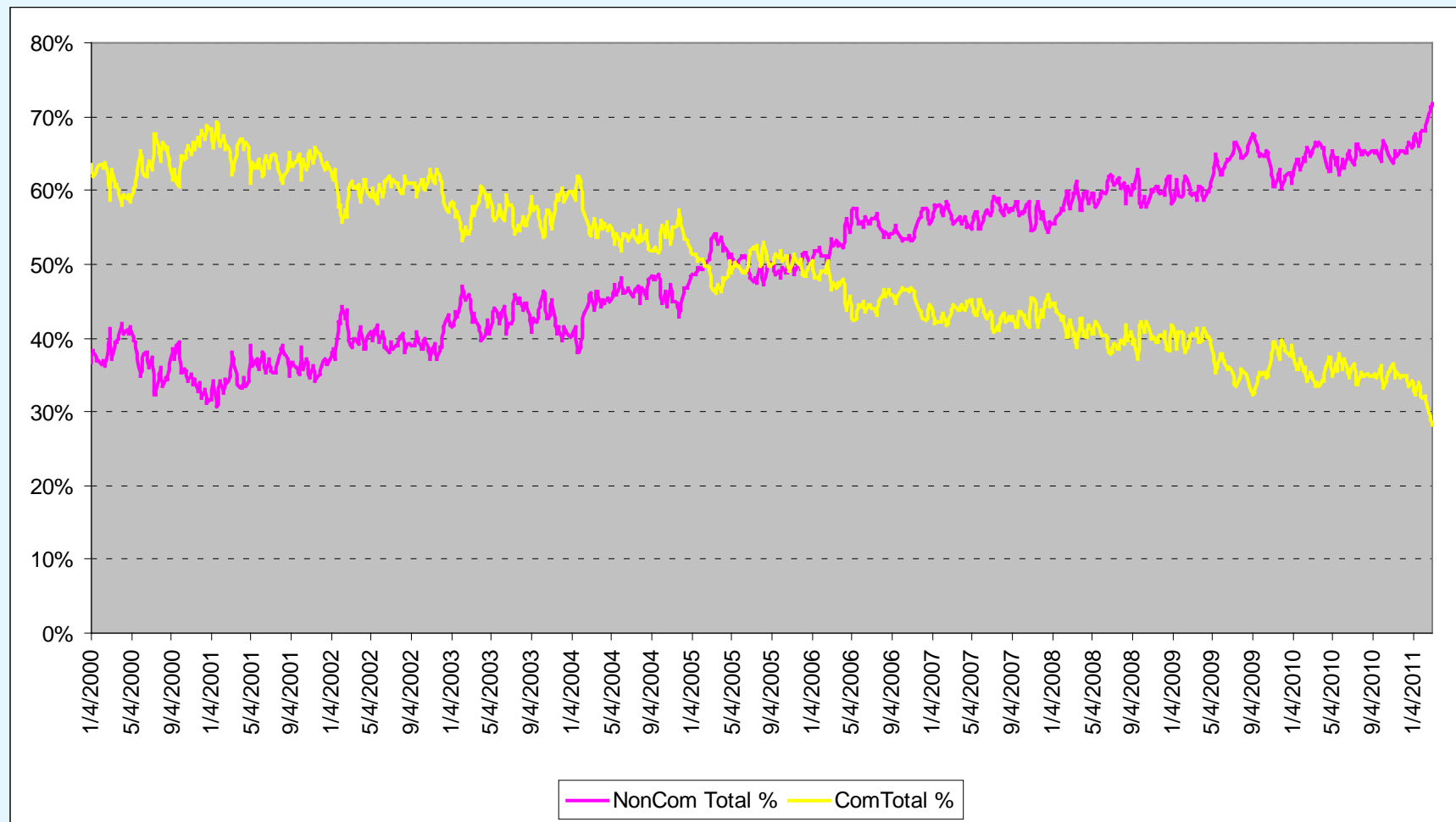
Drive the **DIRECTION** of gas prices



Drive the **MAGNITUDE** of gas prices

HEDGE FUNDS & SPECULATIVE TRADING

Traders in Charge



-  Total of Non-Commercial Long + Short Market Participants by percentage
-  Total of Commercial Long + Short Market Participants by percentage

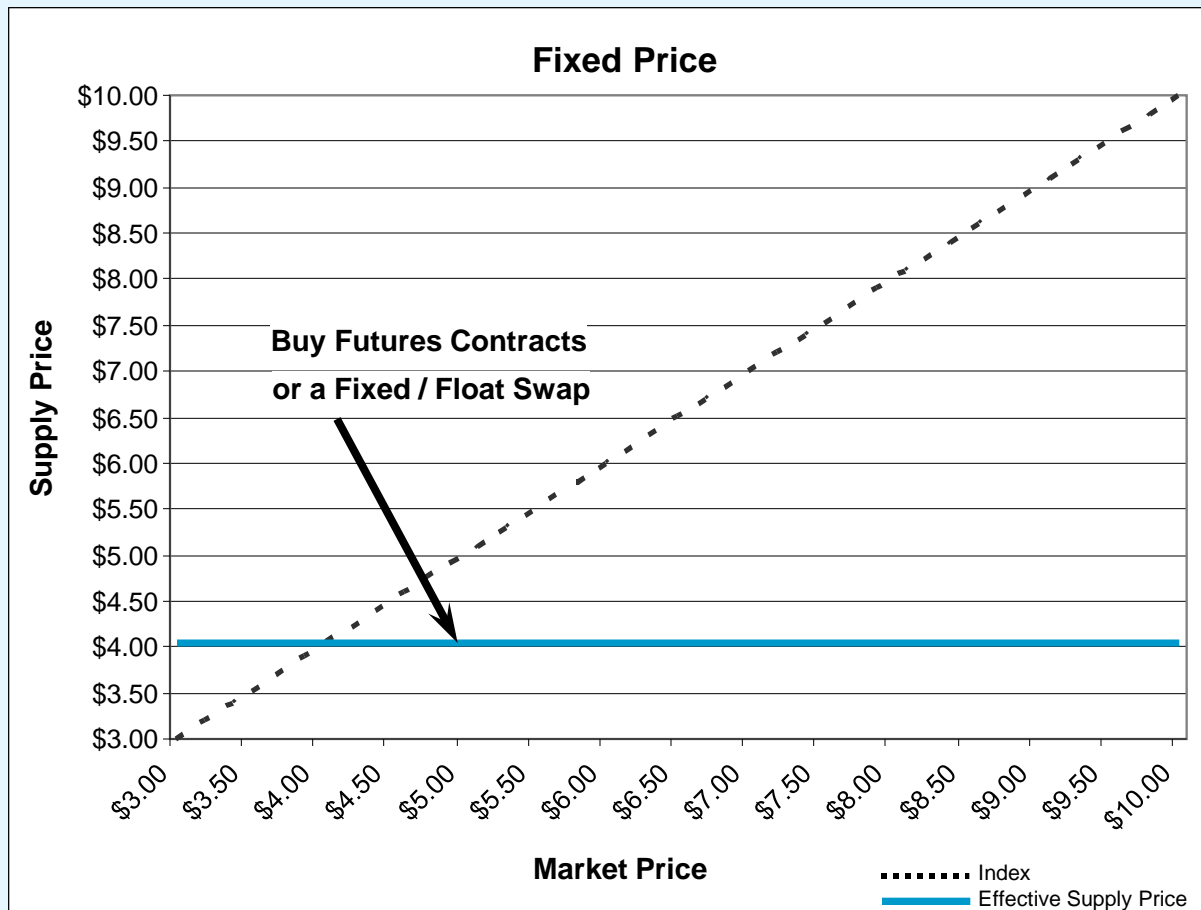
Why should a company hedge?



- **Reduce volatility of gas supply**
- **Neutralize the adverse effects of volatility**
- **Gain price certainty**
- **Not to beat the market**

Fixed Price Swaps (and Futures)

Swaps and futures create a fixed price. Regardless of whether the Index is more than or less than the fixed price, the supply price will not change.

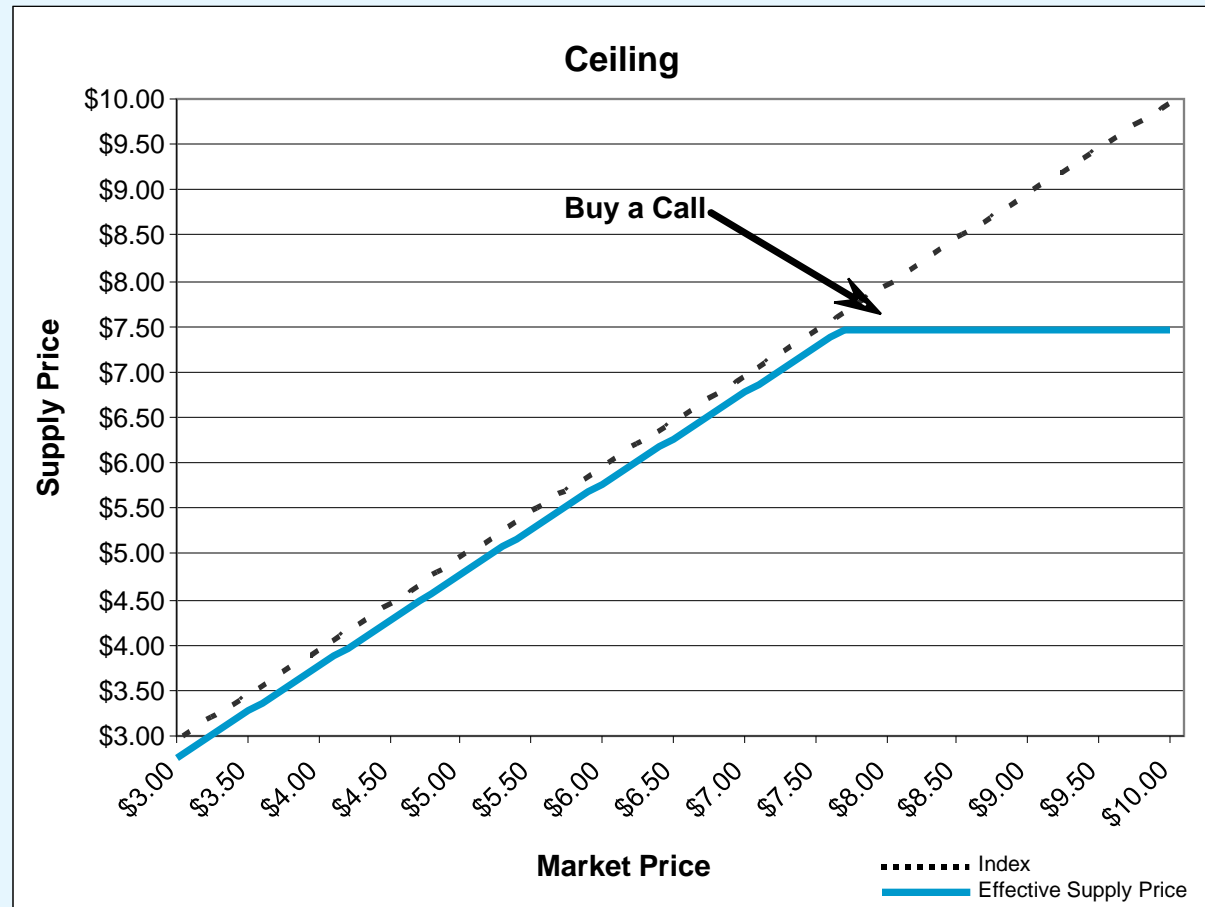


GAS PRICE HEDGING

Ceiling Price



Call options create a ceiling price. When the index is below the ceiling price, the supply price will follow the index price downward, plus the premium paid for the call option.

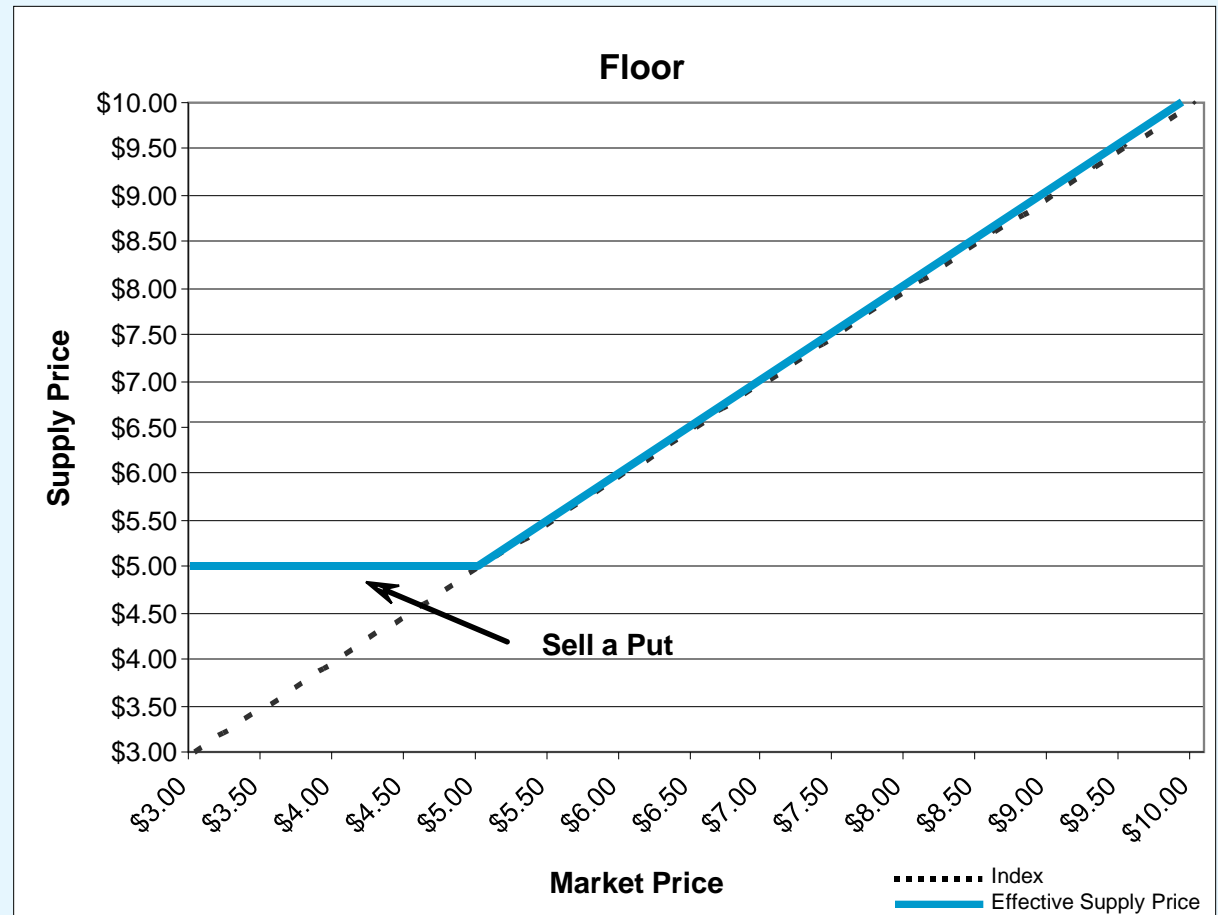


GAS PRICE HEDGING

Floor Price



Put options create a floor price. When the index is above the floor price, the supply price will follow the index price upward, less the premium received for the put option.



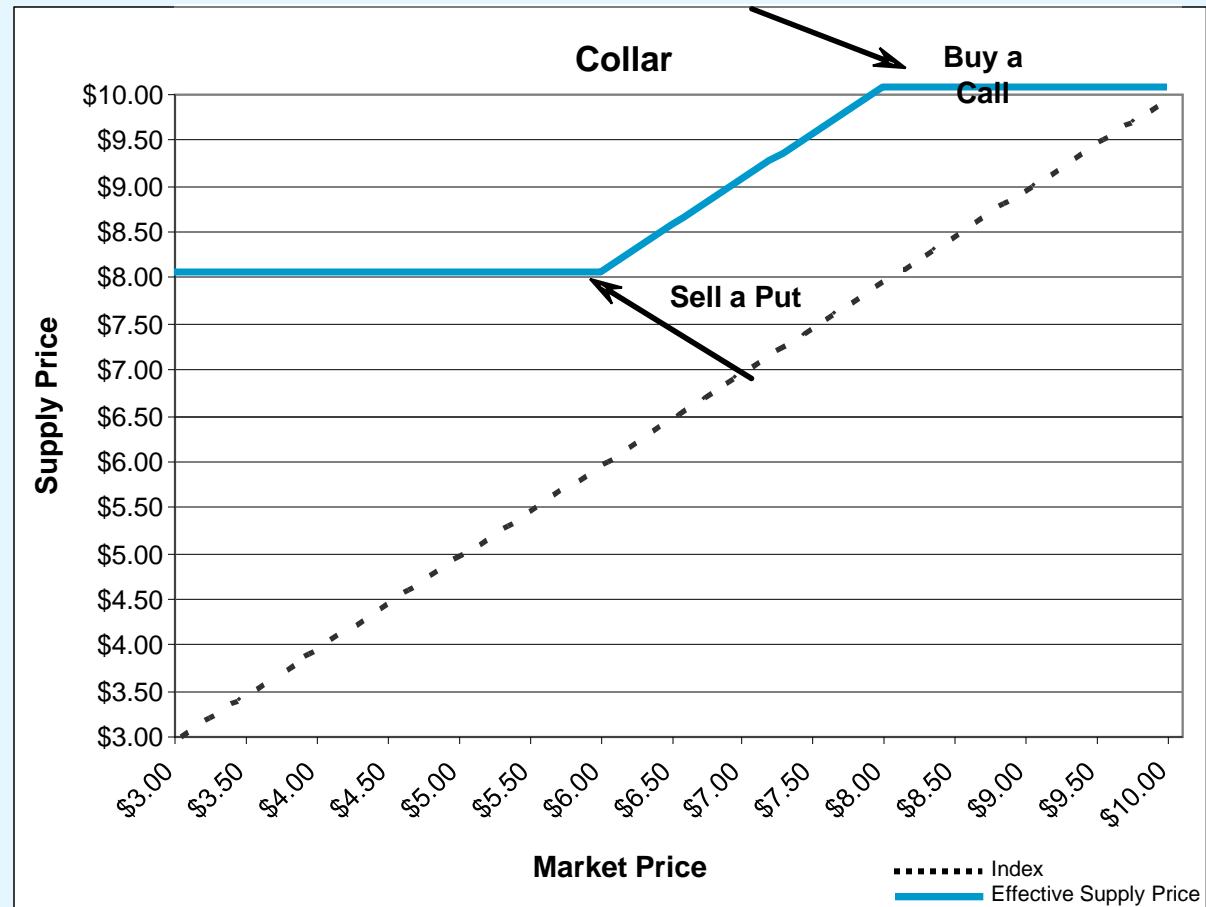
GAS PRICE HEDGING

Collar (2008)

Collars combine the call and put options to create a band within which prices may fluctuate.

The option volumes are equal. When the call and put option premiums offset each other (costless collar), the supply price between the ceiling and floor is at Index.

When the call option premium is greater than the put option premium, the supply price between the ceiling and floor will be greater than Index.



GAS PRICE HEDGING Collar (2008)



OUCH!!!!

High commodity prices

- Gold hit record
- Silver hit record
- Food at all time high
- Crude hit \$110.00 barrel
- Gasoline \$4.00 a gallon
- Industrial metals at high
- Timber at high
- Because it's the right thing to do.....

Why Hedge?



- Very low interest rates but your company **STILL** enters into interest rate swaps
- Weak dollar but your company will **STILL** hedge forward foreign exchange
- Your company still hedges other commodities
- So why not hedge natural gas?

GAS PRICE HEDGING

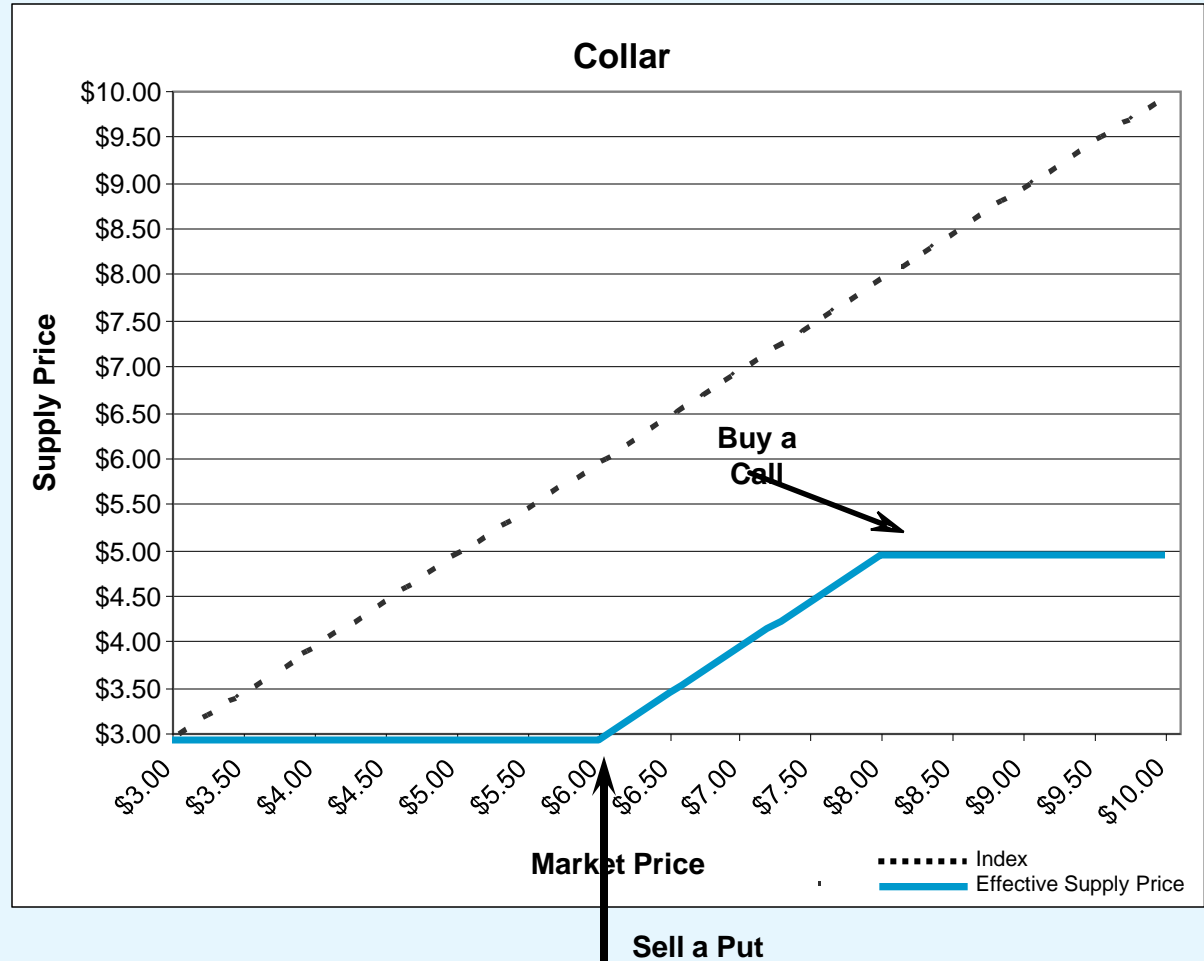
Collar (2011)



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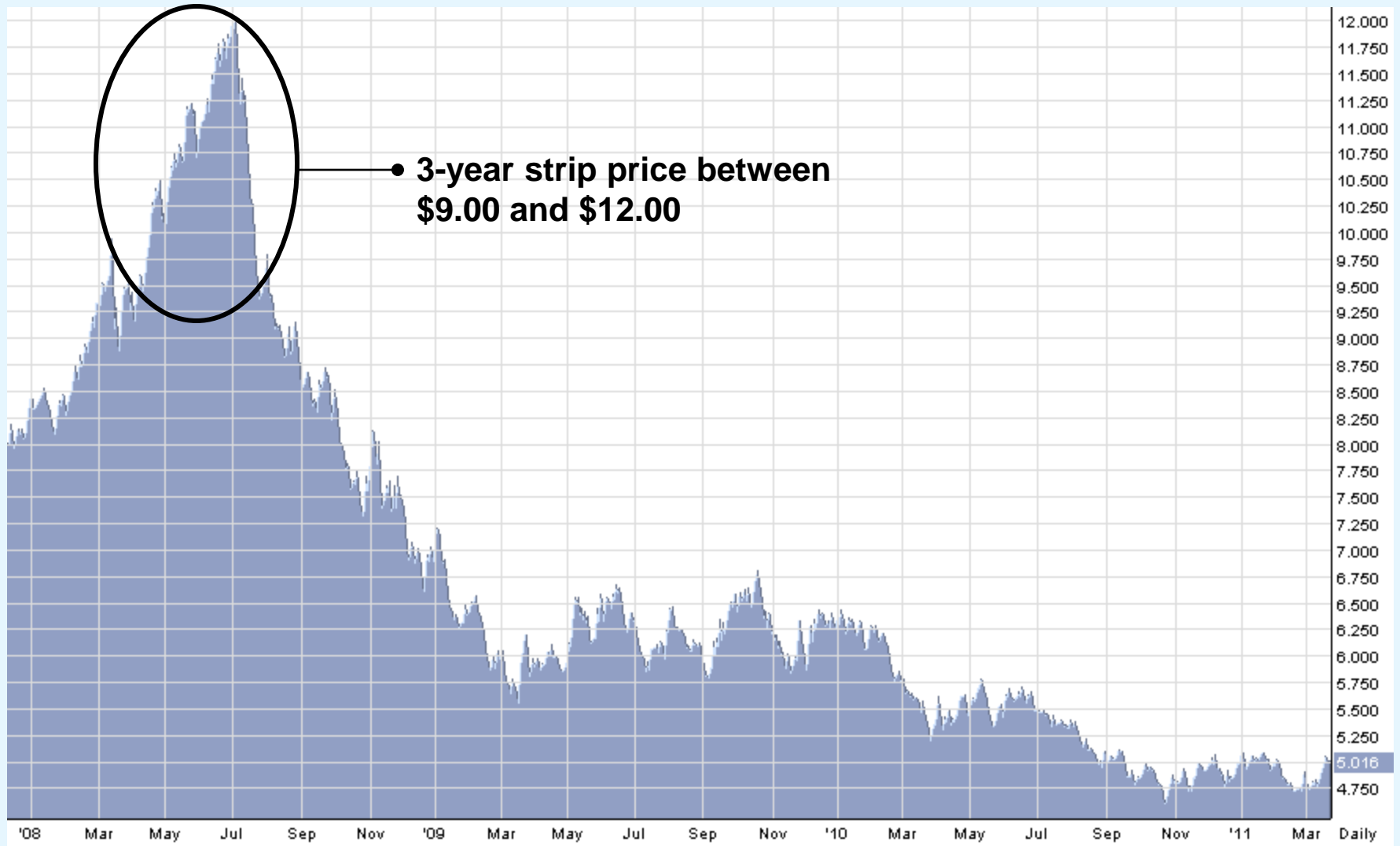


5.600
5.400
5.200
5.000

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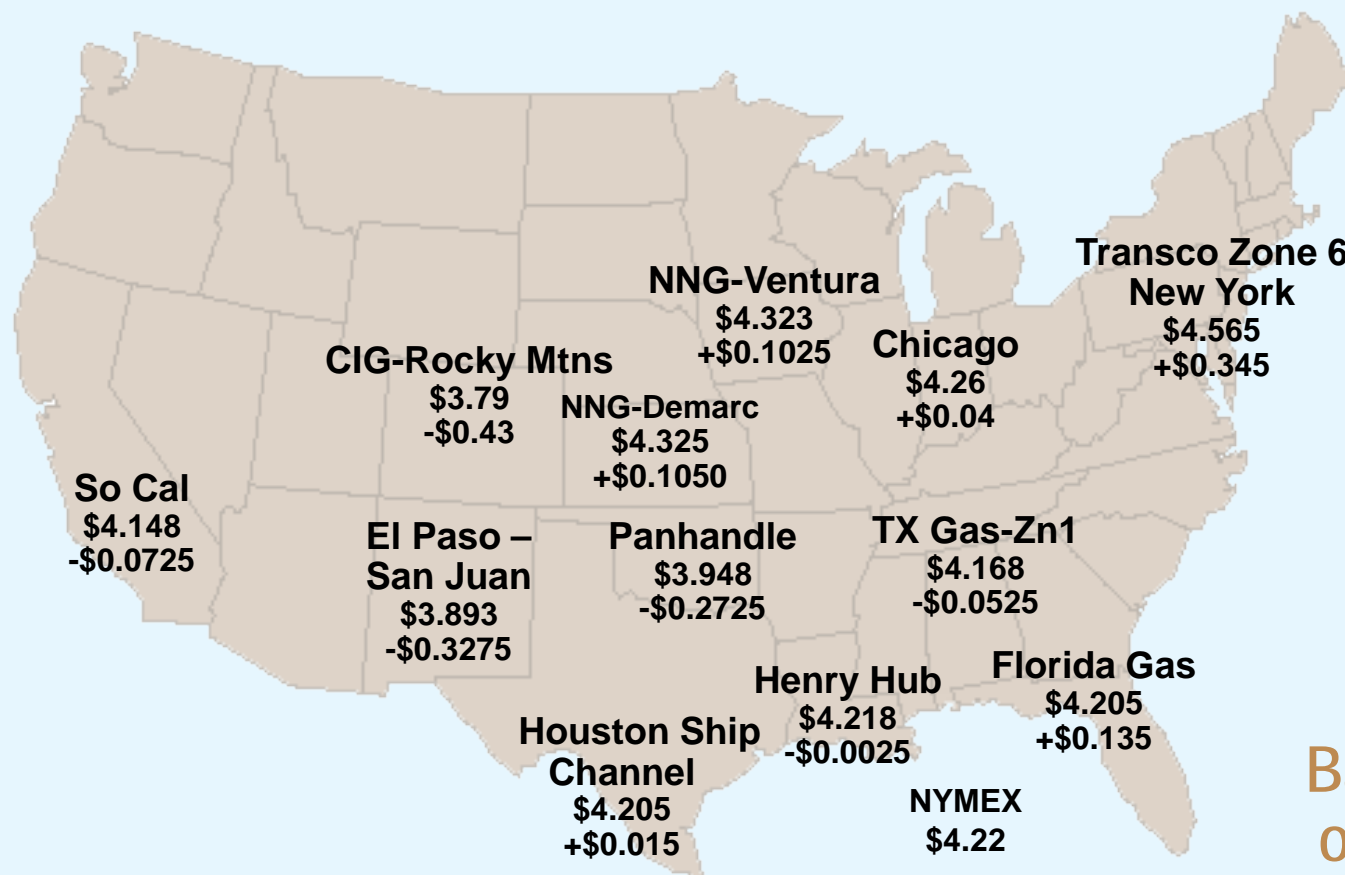
**Do you really need to protect the
downside in this market?**

Natural Gas: 3-Year Strip Prices



5.600
5.400
5.200
5.000

BASIS = Cash (Spot) Price - Futures Price



May 2011
Basis Quotes
on 4/15/2011

Why should a company hedge?



- Just because prices are currently low they will not always stay this way
- Volatility is here to stay – regardless of price level
- Keep volatility smooth and prices low for consumers
- If injections follow the five year average we'll end the season at 3.649 TCF (This could be deemed as bullish)
- No surprises

Why should a company hedge?



- Funds are net short in the Futures market
- What happens when they cover these positions?
- Rigs are on the decline
- Hot Summer?
- Hurricanes?
- Power Generation
- Coal/Gas Switching
- Natural gas could easily go to \$6.50
- Natural gas could also go to \$3.50

- The Market is driven by financial markets as well as fundamentals
- The funds are still in control
- In 2008 companies over-paid for natural gas and consumers are still paying the price
- Good risk management is still key
- Current low prices will not stay around forever
- Now is a good time to hedge
- Long term contracts and short term contracts are both desirable
- Portfolio approach is essential

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